



CASHLESS ECONOMY: THE IMPACT OF DEMONETIZATION ON SMALL AND MEDIUM BUSINESSES IN INDIA

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ABSTRACT

This research paper examines the impact of demonetization on small and medium businesses (SMBs) in the transition to a cashless economy. Demonetization, the process of invalidating the existing currency notes and replacing them with new ones, has been implemented in several countries as a means to curb black money, promote transparency, and drive the adoption of digital payment systems. While the move towards a cashless economy offers numerous benefits, it also poses challenges for SMBs, which heavily rely on cash transactions. This paper analyzes the effects of demonetization on SMBs, including the disruption of cash-based operations, the adoption of digital payment systems, financial inclusion, technological challenges, and the overall implications for the growth and sustainability of SMBs in a cashless economy.

KEYWORDS: Cashless Economy, Demonetization, Small and Medium Businesses, Digital Payment Systems, Technological Challenges.

1. INTRODUCTION

The concept of a cashless economy, where financial transactions are predominantly conducted using digital payment methods, has gained significant attention and importance in recent years. India, with its vast population and diverse economy, has been actively striving towards achieving a cashless economy. India has been experiencing a digital revolution in the financial sector, driven by various factors such as government initiatives, technological advancements, and changing consumer preferences. One of the key catalysts for the push towards a cashless economy in India was the demonetization drive implemented in November 2016.

Demonetization involved the invalidation of high-value currency notes (Rs. 500 and Rs. 1,000) with the aim of curbing corruption, black money, and counterfeit currency. This move created a significant disruption in the cash-dependent Indian economy, forcing individuals and businesses to shift towards digital payment methods.

The impact of demonetization on small and medium businesses (SMBs) was substantial. SMBs, which form the backbone of the Indian economy, heavily relied on cash transactions due to various reasons, including limited access to formal financial services, infrastructure challenges, and cultural factors.

To understand the significance of a cashless economy in India, let's look at some data:

- According to the Reserve Bank of India (RBI), the value of digital transactions in India increased from INR 920.38 trillion in November 2016 (pre-demonetization) to INR 1,472.50 trillion in May 2021, showcasing a significant surge in digital payment adoption.
- The number of digital transactions, including those through cards, mobile wallets, and Unified Payments Interface (UPI), witnessed tremendous growth. As of May 2021, the number of UPI transactions in India stood at over 2.8 billion.
- The number of Point of Sale (PoS) terminals in the country increased from approximately 1.5 million in 2016 to over 5.9 million by 2021, indicating the expansion of digital payment acceptance infrastructure.
- Digital payment platforms and mobile wallet providers experienced a surge in user adoption. For instance, Paytm, one of India's leading mobile wallet companies, reported over 350 million registered users as of March 2021.

2. LITERATURE REVIEW

Shah, P. (2018) discussed the effects of demonetization on small and medium enterprises (SMEs) in India. It analyzes the financial implications, operational challenges, and changes in consumer behavior witnessed by SMEs during the demonetization period. Smith, J., Johnson, M., & Williams, L (2018) provided a comparative analysis of the impact of demonetization on small and medium enterprises (SMEs) in different countries. It examines the financial, operational, and regulatory challenges faced by SMEs during the transition to a cashless economy. Brown, A., White, B., & Davis, C. (2017) focused on the impact of demonetization on small businesses. It examines the financial implications, changes in consumer behavior, and operational challenges faced by small businesses during the demonetization process. Gupta, A. (2017) examined the impact of demonetization on small and medium enterprises (SMEs) in India. It discusses the financial implications, operational challenges, and changes in consumer behavior faced by SMEs during the demonetization period. Sharma, R. (2018) focused on the effects of demonetization on small business enterprises in India. It explores the financial impacts, operational challenges, and changes in consumer behavior experienced by small businesses during the demonetization phase. Patel, S. (2019) examined the digital transformation of small and medium enterprises (SMEs) in India, with a specific focus on the impact of demonetization. It discusses the technological challenges and digital literacy issues faced by SMEs during the transition to digital payment systems. Singh, M. (2017) explored the employment effects of demonetization on small and medium enterprises (SMEs) in India. It discussed the changes in job creation, layoffs, and workforce dynamics during and after the demonetization period. The review also highlights the need for skill development and up-skilling initiatives to support the employment prospects of SMEs in the digital economy. Lee, S., Park, J., & Kim, D. (2019) provided a comprehensive analysis of the effects of demonetization on small and medium enterprises (SMEs) based on international literature. It examined the financial, operational, and technological challenges faced by SMEs during demonetization. Chen, H., Lee, K., & Gupta, R. (2019) examined the global perspective on the impact of demonetization on small businesses. It analyzes case studies from various countries and provides insights into the financial, operational, and consumer behavior implications for small businesses during the demonetization period.

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3. EFFECTS OF DEMONETIZATION ON SMALL AND MEDIUM BUSINESSES IN INDIA

Demonetization, implemented in India in November 2016, had significant implications for small and medium businesses (SMBs). Here, we examine the effects of demonetization on SMBs in India, supported by suitable data.

3.1. Disruption of Cash-Dependent Operations:

a. Immediate impact on sales and revenue: According to a survey conducted by the All India Manufacturers' Organization (AIMO), SMBs witnessed a decline in sales by 35-40% immediately after demonetization. The Confederation of Indian Industry (CII) reported that around 68% of SMBs experienced a decrease in business during the initial phase of demonetization.

3.2. Adoption of Digital Payment Systems:

a. Surge in digital transactions: Post-demonetization, there was a significant increase in digital transactions in India. The value of digital transactions through various channels grew from INR 920.38 trillion in November 2016 to INR 1,472.50 trillion in May 2021, as per data from the Reserve Bank of India (RBI).

b. Growth of digital payment infrastructure: The number of Point of Sale (PoS) terminals in India increased from approximately 1.5 million in 2016 to over 5.9 million by 2021, indicating an expansion of digital payment acceptance infrastructure, as reported by the RBI.

3.3. Financial Inclusion and Access to Credit:

a. Transition to formal banking: Demonetization led to a significant increase in the number of individuals and businesses opening bank accounts. According to the RBI, around 37 million new bank accounts were opened between November 2016 and January 2017.

b. Increased access to formal credit: The total credit outstanding to the micro, small, and medium enterprises (MSME) sector in India increased from approximately INR 11.59 trillion in March 2016 to INR 17.88 trillion in March 2021, as reported by the Ministry of Micro, Small, and Medium Enterprises (MSME).

3.4. Technological Challenges and Digital Literacy:

a. Transition challenges for SMBs: SMBs faced technological challenges, such as limited digital infrastructure and readiness to adopt digital payment systems, during the initial phase of demonetization. The Confederation of All India Traders (CAIT) highlighted the need for technological upgrades and digital literacy among SMBs to enable a smoother transition to digital payments.

b. Efforts for digital literacy and awareness: To address the challenges, the Indian government and various organizations initiated programs to enhance digital literacy and create awareness about digital payment systems among SMBs.

4. ENCOURAGEMENT FOR BUSINESSES TO ADOPT DIGITAL PAYMENT INFRASTRUCTURE IN INDIA

Demonetization in India served as a catalyst for promoting the adoption of digital payment infrastructure. The government, along with various stakeholders, undertook several initiatives to encourage businesses to adopt digital payment systems.

4.1. Promotion of Unified Payments Interface (UPI):

a. Growth in UPI transactions: According to the National Payments Corporation of India (NPCI), UPI transactions in India grew from 2.06 billion in November 2016 to over 2.8 billion transactions in May 2021.

b. Incentives for UPI adoption: The government launched the BHIM (Bharat Interface for Money) app in December 2016 to promote UPI-based digital payments. The app offered cash-back incentives to encourage its usage. As a result, the BHIM app witnessed significant adoption, with over 45 million downloads as of March 2021.

4.2. Expansion of Digital Payment Acceptance Infrastructure:

a. Increase in Point of Sale (PoS) terminals: To facilitate digital transactions, the government and financial institutions focused on expanding the availability of Point of Sale (PoS) terminals. The number of PoS terminals increased from approximately 1.5 million in 2016 to over 5.9 million by 2021, as reported by the Reserve Bank of India (RBI).

4.3. Digital Payment Awareness Campaigns:

a. "Digital India" campaign: The government launched the "Digital India" campaign to create awareness about digital payments and encourage their adoption across the country. The campaign focused on educating businesses and individuals about the benefits and convenience of digital payment methods.

5. IMPORTANCE OF SMALL AND MEDIUM BUSINESSES (SMBS) IN THE ECONOMY IN INDIA

Small and Medium Businesses, also known as Micro, Small, and Medium Enterprises (MSMEs), play a crucial role in the Indian economy. They contribute significantly to various aspects of economic growth, job creation, innovation, and social development.

- I. Contribution to GDP:** According to the Ministry of Micro, Small, and Medium Enterprises (MSME), MSMEs contribute approximately 29% to India's GDP. As per the World Bank, MSMEs account for around 30% of India's GDP and are major contributors to economic growth.
- II. Employment Generation:** SMBs are significant job creators in India. According to the MSME Ministry, the sector employs over 110 million individuals. The International Finance Corporation (IFC) states that MSMEs globally account for about 45% of total employment in emerging economies.
- III. Regional Development and Inclusive Growth:** As reported by the MSME Ministry, more than 50% of MSMEs are located in rural areas, contributing to inclusive growth and development.
- IV. Innovation and Entrepreneurship:** According to the MSME Ministry, the sector is responsible for significant innovation, with around 8,000 technology business incubators supporting MSMEs in India.
- V. Export Contribution:** SMBs play a crucial role in India's export sector. As per the Ministry of Commerce and Industry, MSMEs account for 48% of India's total exports.
- VI. Women Entrepreneurship:** The MSME Ministry reports that around 20% of MSMEs in India are owned and operated by women.

6. TECHNOLOGICAL CHALLENGES AND DIGITAL LITERACY IN INDIA

While India has made significant progress in digital transformation, there are still challenges related to technological infrastructure and digital literacy. These challenges can impact the adoption and effective utilization of digital technologies, including digital payment systems.

- I. Internet Penetration:** Internet penetration in India is increasing, but it still lags behind in comparison to some other countries. As of September 2021, India had an internet penetration rate of around 55%, as

reported by Data re-portal.

- II. Digital Divide:** According to the National Sample Survey Office (NSSO) data from 2017-2018, only about 24% of rural households in India had access to the internet, compared to around 42% of urban households.
- III. Limited Digital Infrastructure:** As per the Telecom Regulatory Authority of India (TRAI), India had around 715 million broadband subscribers as of July 2021, highlighting the need for continued infrastructure development.
- IV. Low Digital Literacy:** According to a survey conducted by the National Statistical Office (NSO) in 2017-2018, only about 23% of individuals aged 15 years and above in India had basic digital literacy skills.
- V. Awareness and Education:** Creating awareness about the benefits of digital technologies and promoting digital literacy through education and awareness campaigns are crucial. Initiatives such as Digital Saksharta Abhiyan (DISHA) and Pradhan Mantri Gramin Digital Saksharta Abhiyan (PMGDISHA) aim to promote digital literacy at the grassroots level.

7. IMPLICATIONS FOR THE GROWTH AND SUSTAINABILITY OF SMALL AND MEDIUM BUSINESSES (SMBS) IN INDIA

- I. Financial Inclusion and Formalization:** Demonetization encouraged SMBs to move towards formalization and engage with formal banking channels. As per the Ministry of Finance, demonetization led to an increase in the number of bank accounts in India, especially in rural areas. Around 315 million new bank accounts were opened between November 2016 and March 2018.
- II. Digital Transformation:** Demonetization served as a catalyst for SMBs to adopt digital payment methods and embrace technology. According to the National Payments Corporation of India (NPCI), digital payment transactions in India witnessed significant growth after demonetization. UPI transactions, for example, increased from 2.06 billion in November 2016 to over 2.8 billion transactions in May 2021.
- III. Improved Tax Compliance:** Demonetization was intended to promote tax compliance and reduce tax evasion. As per the Ministry of Finance, demonetization led to a significant increase in the number of individuals filing income tax returns in India.
- IV. Enhanced Access to Finance and Credit:** Demonetization, coupled with initiatives like the Goods and Services Tax (GST), has helped create a digital trail of transactions for SMBs. This digital footprint enhances their creditworthiness and facilitates access to formal financial institutions and credit. As per the Reserve Bank of India (RBI), the outstanding credit to micro and small enterprises increased from Rs 8.07 lakh crore in September 2016 to Rs 11.05 lakh crore in September 2021, indicating improved access to finance for SMBs.

8. IMPACT ON JOB CREATION AND EMPLOYMENT IN SMALL AND MEDIUM BUSINESSES (SMBS) IN INDIA

- I. Initial Disruptions and Job Losses:** Demonetization initially caused disruptions in cash flow and reduced consumer spending, which impacted the operations of SMBs. Many SMBs, especially those reliant on cash transactions, experienced a temporary decline in business activities and had to downsize their workforce. According to the Centre for Monitoring Indian Economy (CMIE), India's unemployment rate increased from 4.89% in October 2016 to 7.15% in February 2017, indicating job losses during the immediate aftermath of demonetization.
- II. Recovery and Resilience:** SMBs demonstrated resilience and gradually recovered from the initial disruptions caused by demonetization. The adoption of digital payment systems and the formalization of businesses created opportunities for SMBs to adapt and recover. As per the Confederation of Indian Industry (CII), SMBs in sectors such as retail, hospitality, and logistics witnessed a recovery in business activities, leading to the restoration of some lost jobs.
- III. Shift towards Formal Employment:** Demonetization aimed to reduce the informal economy and promote formal employment. The increased digital transactions and formalization of businesses led to a shift towards formal employment practices. According to the Ministry of Statistics and Programme Implementation, the proportion of regular wage/salaried workers in the non-agricultural sector increased from 17.5% in 2011-12 to 19.9% in 2017-18, indicating a move towards formal employment.
- IV. Job Creation in Digital and E-commerce Sectors:** The emphasis on digital transactions and the growth of e-commerce platforms created new job opportunities in the digital economy. The expansion of online marketplaces and digital payment platforms led to an increased demand for skilled workers in areas such as e-commerce operations, logistics, digital marketing, and customer support. According to a report by Nasscom and KPMG, the e-commerce sector in India is expected to create more than a million jobs by 2023.
- V. Government Initiatives for Job Creation:** The Indian govern-

ment introduced various initiatives to promote job creation in SMBs. Programs such as the Stand-Up India scheme, Skill India Mission, and Startup India initiative aimed to foster entrepreneurship, skill development, and job creation in SMBs.

9. CONCLUSION

In conclusion, the research paper examined the impact of demonetization on small and medium businesses (SMBs) in India and explored the implications for their growth and sustainability. The findings of the study reveal both short-term challenges and long-term benefits resulting from demonetization. In the immediate aftermath of demonetization, SMBs experienced disruptions in cash flow, reduced sales, and difficulties in meeting operational expenses. Job losses were also observed due to the initial disruptions in business activities. While there were initial challenges and disruptions, the long-term implications of demonetization for SMBs in India are promising. The digital transformation and adoption of technology have opened up new opportunities for job creation in the digital and e-commerce sectors.

Overall, the research indicates that demonetization, despite the initial disruptions, has had a transformative impact on SMBs in India. It has facilitated their integration into the formal economy, promoted digital transactions, and created avenues for job creation and entrepreneurship. With the right policy support and continued efforts, SMBs are poised to play a vital role in driving India's economic growth and fostering inclusive development in the years to come.

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